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SUBJECT: MEXICAN AUTO INDUSTRY ON ROUGH ROAD, SEEKING ROADSIDE ASSISTANCE

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¶1. (SBU) SUMMARY: While the Obama Administration has acted firmly to aid the United States' beleaguered automotive industry, the Mexican auto manufacturers are looking askance at their own government's seemingly lackluster response. In separate conversations, representatives from Mexico's auto industry voiced their cautious optimism to ECONOFF that new car sales will pick up soon, and that the industry will see better negative numbers for the remainder of the year. What would really help, they said, is support from the GOM to boost the domestic market. END SUMMARY.

BAD NUMBERS

¶2. (U) The numbers continue to paint a dismal picture for the auto industry in Mexico. According to the Mexican Automotive Industry Association (AMIA), total production of new cars in Mexico for the first five months of 2009 was 41.7 percent less than the same period in 2008 - just over half a million cars compared to 858,398 the previous year. Mexico exports 80 percent of its manufactured cars; 71 percent of the total cars it produces are exported to the U.S. market. In the first part of 2009, the total number of vehicle exports also fell 41.5 percent from last year, from 683,070 to just under 400,000 cars. Even Mexico's domestic market has dried up - domestic sales dropped 30.6 percent from Jan-May 2008.

A VIEW FROM THE AUTO INDUSTRY

¶3. (U) However, AMIA's President Eduardo Solis is optimistic that the sector has hit bottom, and that we should start seeing 'better negative numbers' beginning in July. Solis told ECONOFF that the U.S. Consumer Confidence Index has been on the upswing for three months in a row, and given a two-month lag, U.S. sales will likely begin to pick up in July. (NOTE: The Index now stands at 54.9, the highest level since September 2008. END NOTE.) Also helpful in boosting U.S. consumption of new cars will be the U.S. government scrappage program - officially the Consumer Assistance to Recycle and Save (CARS) program, signed into law last week by President Obama and scheduled to begin Wednesday, July 1. Solis hastened to add, however, that the auto industry will still end the year in negative numbers, with an anticipated overall 25 percent drop in sales and a 25-30 percent drop in production. He does not foresee positive numbers until the end of 2010.

¶4. (SBU) When asked about the shift in the market demand for more fuel-efficient vehicles, Solis frankly disagreed that such a shift was occurring. Both the U.S. and Mexican governments will have to force such a change, he said, through additional fiscal incentives for consumers and producers as well as programs such as CARS. Even then, the phase-in of such vehicles could not occur until at least 2011. If there is such a shift, Solis assured ECONOFF, the Mexican auto industry will adapt, but it will need help from the Mexican government. The problem in the short-term is that many of Mexico's production platforms were installed within the past few years to manufacture the larger vehicles on American roads - the Chevy Suburban, the Dodge Ram pickup, and the Cadillac Escalade. Given time and incentives, Solis said, Mexico's production platforms can be reconfigured to respond to any shift in demand.

¶5. (SBU) In the United States, Solis pointed out, it is the government that is pushing for better standards. By contrast, in Mexico it is the industry that is pushing the government for improved regulations. For example, only unleaded gasoline (regular - 87 octane, and premium - 91 octane) is available in most parts of Mexico today. Ultra low sulfur (ultra bajo azufre, or UBA) diesel, which is used in lower-emission diesel vehicles, has yet to be introduced and made widely available in Mexico. In order to introduce better technologies to the Mexican market, government support for increased fuel efficiency and lower emissions standards is essential. Unfortunately, the government has neither the understanding of the situation nor the fiscal means to address such a need, he

lamented.

¶6. (SBU) On the issue of used cars, Solis stated emphatically that most used vehicles from the United States have a deleterious effect on new car sales in Mexico. Many of these cars have been identified as at the end of useful life in the United States, yet they are shipped to Mexico where they gain a second life. NAFTA, Solis said, was not intended to be used as a means to send garbage to each other. Moreover, the impact on new car sales is indirect but important, as they depress the market in a rollover effect that eventually prevents a potential purchaser of a new car from trading in his two- to three-year old car. Solis, a former NAFTA negotiator for Mexico, insisted that he is for the trade of used cars but that we must trilaterally negotiate a protocol of common trade for such vehicles.

GM'S OUTLOOK

¶7. (SBU) In a separate meeting with ECONOFF, GM Director of Government Relations Mauricio Kuri echoed many of Solis's comments. The GOM, he said, needs to send the right signal that it supports the automotive industry in Mexico, and create programs that work. 70 percent of new car sales in Mexico, he pointed out, are conducted with financing. Unfortunately, that credit has dried up or the standards are now much higher so as to depress the domestic market. Kuri was critical of the 2 billion peso (US$ 154 million) government pro-employment program, meant to support industries with temporary plant shutdowns. GM has had rolling shutdowns of its plants in Mexico, but as it kept its workers on the payroll, it did not qualify for the government program. These programs, Kuri complained, have such crazy rules that are so complicated that they actually hurt rather than help. (NOTE: Local press reports that Volkswagen was the first auto manufacturer in Mexico to avail itself of the government pro-employment program, receiving 18.6 million pesos (US$ 1.4 million) on June 9, and is seeking another package of 21.7 million pesos (US$ 1.6 million). The press also cites sources that say GM will soon follow. END NOTE.)

¶8. (SBU) Kuri commented on GM's restructuring plan. Plants

were closed and jobs were cut in the United States and Canada, he said, to reduce labor costs. GM's plants in Mexico are more modern and cost-effective than their northern counterparts and will stay open to make the most of these efficiencies as well as Mexico's competitive advantage in lower labor costs. Kuri said that GM's green technology production had remained in the United States, while Mexico had focused on producing GM's pick-up and SUV lines. He did not say that the production of smaller, more fuel-efficient cars would shift to Mexico from the United States, but he acknowledged that GM's Mexico plants have the requisite technology to produce the next generation of cars. The bottom line, he concluded, is that Mexico's GM branch is well-placed to be very profitable to the company.

FORD

¶9. (SBU) Separately, Raul del Campo, Ford Motor Company's Director of Government Relations, bragged to the Embassy's Economic Specialist that Ford is the only U.S. auto manufacturer that has not required a bailout program from the U.S. government, and that it could emerge from the current crisis as the largest U.S. automaker (NOTE: GM had 18.6 percent of the U.S. market in the first quarter of 2009 to Ford's 14.7 percent. END NOTE). He claimed that Ford's production will be able to adapt to any shift in market demand since their platforms are flexible. However, del Campo also insisted on a scrappage program to increase domestic sales.

¶10. (U) Since these meetings, ECONOFF has learned that the Secretariat of the Economy is expected to announce an incentive program in July. It is still developing the plan, but it is considering funneling US$ 60 million to incentivize the sale of new vehicles in Mexico, either through a tax deduction for the purchase of a new vehicle, the elimination of the tax on new vehicles (ISAN), or a direct economic

support to auto production plants and distributors. However, industry representatives are arguing in support of a scrappage program similar to CARS.

¶11. (SBU) COMMENT: All indications are that the Mexican auto industry will recover. However, much depends on circumstances beyond its control - consumer confidence in the U.S., USG incentives for new car sales, and decisions on whether to out-source production to Mexico. As for the decision over which it holds some sway - that of the GOM to incentivize new car sales in Mexico - it appears to be making some headway, but any program must be simple and accessible in order for it to be truly effective. Post will continue to monitor developments in the government domestic market incentive program and the industry's response.

¶12. (SBU) A final note on used cars in Mexico; something that has been largely overlooked in the public debate in Mexico over the importation of used vehicles from the United States is the fact that it makes vehicles affordable for an entire sector of the Mexican population. The economic contribution of this mobile workforce is difficult to measure but according to our counterparts in the border consulates, is significant. END COMMENT.

FEELEY